Nos. 14-614 & 14-623

IN THE

Supreme Court of the United States

W. KEVIN HUGHES, *et al.*,
Petitioners,

v.

TALEN ENERGY MARKETING, LLC
(f/k/a PPL ENERGYPLUS, LLC), *et al.*,
Respondents.

CPV MARYLAND, LLC,
Petitioner,

v.

TALEN ENERGY MARKETING, LLC
(f/k/a PPL ENERGYPLUS, LLC), *et al.*,
Respondents.

On Writs of Certiorari to the United States Court of Appeals for the Fourth Circuit

BRIEF FOR AMERICAN ELECTRIC POWER COMPANY, INC., AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

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BRIEF FOR AMERICAN ELECTRIC POWER COMPANY, INC., AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

American Electric Power Company, Inc., respectfully submits this brief as *amicus curiae* in support of respondents.[1]

[1] No party or counsel for a party authored this brief in whole or in part, or made a monetary contribution intended to fund the brief's preparation or submission. No one other than *amicus*, its members, or its counsel made any such monetary contribution. The parties have filed letters granting blanket consent to *amicus* briefs.

INTEREST OF *AMICUS CURIAE*

American Electric Power Company, Inc. (AEP) is a public utility holding company. Through its affiliates, it is one of the country's largest investor-owned utilities, serving parts of eleven States and more than five million American customers. AEP's service territory covers 197,500 square miles in Arkansas, Indiana, Kentucky, Louisiana, Michigan, Ohio, Oklahoma, Tennessee, Texas, Virginia and West Virginia. AEP's customers are served by one of the world's largest transmission and distribution systems, with more than 40,000 miles of transmission lines and more than 215,000 miles of distribution lines. Among AEP's affiliates are transmission-, distribution-, and generation-owning members of PJM serving customers in parts of five States in the PJM region. They include both utilities and a power generator in the PJM region.

This case involves the Federal Power Act's (FPA's) division of authority between federal regulators—who have jurisdiction over wholesale rates—and state regulators—who have jurisdiction over retail rates. AEP and its affiliates sell energy into, and purchase energy from, the wholesale energy and capacity markets regulated by FERC, and they also participate in proceedings before state public utilities commissions concerning retail rates charged to consumers. AEP thus has a strong interest in this case because the company and its subsidiaries regularly navigate the balance struck in the FPA between federal and state authorities.

SUMMARY OF ARGUMENT

The Federal Power Act draws a bright line between what States may regulate and what they may not.

The State in this case crossed that line. It forced local electric distribution companies to enter into a so-called contract for difference (CfD) with a generator. It required that generator to sell its energy and capacity into markets administered by PJM Interconnection, LLC. And it commanded the generator and distribution companies to make payments to each other, depending on the difference between the price set in the CfD and the price obtained in the PJM market. By these actions, the State dictated a wholesale rate—the amount of compensation that the generator receives from selling its power into the PJM markets. And because the FPA preempts state action aimed directly at wholesale rates, it preempts the State's actions in this case.

In ruling the CfDs in this case preempted, however, this Court need not—and should not—address whether the FPA preempts an entirely different type of contract: a power purchase agreement. Power purchase agreements have been around a long time, since before the enactment of the FPA. They are agreements by one party to purchase power from another; for example, a utility might agree to purchase from a generator all of the power generated by a certain power plant. The typical power purchase agreement is a voluntary agreement between private parties who freely negotiate its terms, including the amount the generator will receive in exchange for title to the power.

There is thus no state action in either the negotiation or the formation of a private power purchase agreement. To the extent there is any state action at all, it occurs only when a state commission decides whether to allow the utility that purchased the power to pass on the costs and revenues of the

agreement to retail ratepayers. That exercise of state power, however, is traditionally directed only at retail rates and is therefore permissible.

In short, private power purchase agreements present issues distinct from those in this case. This Court should hold that the FPA preempts the state-ordered CfDs here. But it should not issue an opinion that casts doubt on private power purchase agreements or the traditional power of state commissions to permit retail-rate recovery of their costs.

ARGUMENT

I. STATE ACTION MANDATING CONTRACTS FOR DIFFERENCE IS PREEMPTED.

A. The Federal Power Act Preempts State Action Aimed Directly At Wholesale Rates.

The Supremacy Clause of the Federal Constitution establishes the supremacy of federal law over state law. It provides that "the Laws of the United States * * * shall be the supreme Law of the Land * * * , any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." U.S. Const. art. VI, cl. 2. Because federal law is supreme, Congress may "preempt, *i.e.*, invalidate, a state law through federal legislation." *Oneok, Inc.* v. *Learjet, Inc.*, 135 S. Ct. 1591, 1595 (2015).

Only "[s]tate" action is subject to preemption. U.S. Const. art. VI, cl. 2. That is because the Supremacy Clause is a federalist provision, addressed to the relationship between our "two sovereigns"—"the National and State Governments." *Arizona* v. *United States*, 132 S. Ct. 2492, 2500 (2012). Absent "a *state* law, rule, or other *state* action," the doctrine of

preemption has no application. *Oneok*, 135 S. Ct. at 1595 (emphasis added); *see also PLIVA, Inc.* v. *Mensing*, 131 S. Ct. 2567, 2573 (2011) ("Pre-emption analysis requires us to compare federal and *state* law." (emphasis added)).

The "ultimate touchstone in every pre-emption case" is the intent of Congress. *Altria Grp., Inc.* v. *Good*, 555 U.S. 70, 543 (2008) (internal quotation marks omitted). In this case, the FPA "does not refer expressly to pre-emption." *Oneok*, 135 S. Ct. at 1595.[2] But the FPA makes Congress's preemptive intent clear in a different way: It draws a "bright line" between federal and state jurisdiction over electricity. *Nantahala Power & Light Co.* v. *Thornburg*, 476 U.S. 953, 966 (1986) (internal quotation marks omitted); *see also Oneok*, 135 S. Ct. at 1599-1600.

That line appears in 16 U.S.C. § 824(b). Section 824(b) gives FERC jurisdiction over, among other things, "the sale of electric energy at wholesale in interstate commerce." 16 U.S.C. § 824(b)(1). At the same time, it reserves to the States jurisdiction over "any other sale of electric energy." *Id.* Section 824(b) thus divides sales of electricity into wholesale sales and "any other" (*i.e.*, retail) sales. And it places wholesale sales within FERC's exclusive jurisdiction, beyond the authority of States to regulate. *See Nantahala Power*, 476 U.S. at 966.

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[2] The "relevant provisions" of the FPA and the Natural Gas Act "are in all material respects substantially identical." *Ark. La. Gas Co.* v. *Hall*, 453 U.S. 571, 577 n.7 (1981) (internal quotation marks omitted). Thus, it is well established that "decisions interpreting the pertinent sections of the two statutes" may be cited "interchangeably." *Id.*

Other sections of the FPA flesh out the scope of FERC's exclusive jurisdiction over wholesale sales. Section 824d, for example, requires that "[a]ll rates and charges made, demanded, or received * * * for or in connection with" wholesale sales "be just and reasonable." 16 U.S.C. § 824d(a). And § 824e authorizes FERC to "determine the just and reasonable rate" when a wholesale rate is "unjust, unreasonable, unduly discriminatory or preferential." *Id.* § 824e(a). Under the FPA, therefore, FERC's exclusive jurisdiction over wholesale *sales* encompasses the power to regulate wholesale *rates*. *See Nantahala Power*, 476 U.S. at 966.

The "'significant distinction' for purposes of preemption," then, is the distinction between state "'measures aimed directly at interstate purchasers and wholesales for resale, and those aimed at' subjects left to the States to regulate." *Oneok*, 135 S. Ct. at 1600 (emphasis omitted) (quoting *N. Nat. Gas Co.* v. *State Corp. Comm'n of Kan.*, 372 U.S. 84, 94 (1963)). If the state action in question is aimed directly at *wholesale* sales or rates, it is preempted by the FPA. If, instead, the state action in question is aimed directly at *retail* sales or rates, it is not preempted.

B. This Case Involves State Action Aimed Directly At Wholesale Rates.

This case involves CfDs dictated by the State of Maryland. The CfDs in this case are contracts between a power generator and local electric distribution companies. Although the State itself is not a party to these CfDs, the State controlled both who the contracting parties would be and what they would be contracting for.

As to the parties: The State first "solicited proposals for the construction of a new power plant" and selected CPV Maryland, LLC, as the winning bidder. Pet. App. 12a.[3] The State then ordered various distribution companies to enter into twenty-year CfDs with CPV. *Id.* Thus, the State controlled who was party to the CfDs, selecting CPV to be on one side and ordering specific distribution companies to be on the other.

As to the contract terms: The State dictated the obligations of both CPV and the distribution companies. The State required CPV, as the winning bidder, to build a new plant and sell that plant's energy and capacity into the PJM markets. *Id.* The State also set the price of each CfD, and pegged payments under each CfD to the difference between the CfD's state-set price and the clearing price in those markets. *Id.* at 12a-13a. If the state-set price turned out to be *higher* than the clearing price, the distribution companies had to pay CPV the difference. *Id.* at 12a. And if the state-set price turned out to be *lower* than the clearing price, CPV had to pay the distribution companies the difference. *Id.* at 12a-13a. In this way, the State's action guaranteed that CPV would always receive the state-set price—no more, no less—for selling electricity at wholesale into the PJM markets.

The State's actions in this case are preempted by the FPA. The amount of compensation a generator receives for selling energy or capacity into the PJM markets is a wholesale rate. Here, by controlling the

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[3] "Pet. App." citations refer to the petition appendix in No. 14-623.

parties to, and terms of, the CfDs, the State dictated the amount of compensation that CPV would receive for selling energy and capacity into the PJM markets. The State's actions were therefore aimed directly at wholesale rates. And because wholesale rates fall within FERC's exclusive jurisdiction, the State's actions are preempted by the FPA. The Fourth Circuit's decision should be affirmed.

II. IN HOLDING THAT THE STATE ACTION HERE IS PREEMPTED, THE COURT SHOULD NOT IMPAIR PRIVATE PARTIES' ABILITY TO ENTER VOLUNTARILY INTO POWER PURCHASE AGREEMENTS.

To decide this case, this Court need address only the narrow question before it: whether the FPA preempts state-ordered CfDs, between parties chosen by the State, which guarantee a generator a state-set price for selling electricity at wholesale into the PJM market. In deciding that the FPA preempts such state-ordered CfDs, this Court need not—and should not—address whether the FPA preempts other types of contracts, such as privately negotiated power purchase agreements, voluntarily entered into between generators and distribution companies (or utilities). Because private power purchase agreements involve issues distinct from those presented by state-ordered CfDs, the Court in this case should not issue an opinion that would impair the ability of private actors to enter voluntarily into power purchase agreements and obtain retail-rate recovery of the costs.

A. There Is No State Action When Private Actors Enter Voluntarily Into Power Purchase Agreements.

1. As its name suggests, a power purchase agreement is a bilateral agreement to purchase power. For example, a utility might enter into a power purchase agreement with a generator to purchase the power generated by one of the generator's power plants. If the plant has a capacity of 300 megawatts, title to those 300 megawatts transfers from the generator to the utility. The utility then has the right to decide what to do with those 300 megawatts. It could, among other things, decide to sell that capacity into the PJM market.

Power purchase agreements are nothing new; they were common even before the enactment of the FPA. Back in those days, most utilities were "vertically integrated," which meant that they "constructed their own power plants, transmission lines, and local delivery systems." *New York* v. *FERC*, 535 U.S. 1, 5 (2002). But despite being "self-contained," these utilities often entered into agreements to purchase power from their neighbors. Office of Enforcement, FERC, *Energy Primer: A Handbook of Energy Market Basics* 36 (2015).[4] The purpose of many of those early power purchase agreements was to keep the lights on during an emergency; if, for instance, a plant were to break down unexpectedly, a utility could rely on its power purchase agreement with an adjacent utility to continue supplying power to its customers. *Id.*

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[4] *Available at* http://www.ferc.gov/market-oversight/guide/energy-primer.pdf.

Today, power purchase agreements remain a useful way of transferring title to power from one entity to another. Indeed, FERC has granted sellers of electricity at wholesale the authority to "enter into freely negotiated contracts with purchasers." *Morgan Stanley Capital Grp. Inc.* v. *Pub. Util. Dist. No. 1 of Snohomish Cty.*, 554 U.S. 527, 537 (2008). To obtain such authority, the seller must demonstrate that it lacks market power. *Id.* But once it does, it may make wholesale sales at rates determined by bilateral agreement, and FERC will presume that those rates are just and reasonable. *Id.* at 545-546. Power purchase agreements are in use throughout the Nation's interstate electric system, including in the PJM region.

2. Comparing the CfDs in this case with "traditional bilateral sale[s]," petitioners argue that the two types of contracts are "functionally equivalent." Md. Br. 40 (boldface removed). That is incorrect. The typical power purchase agreement differs from the CfDs at issue in this case in two important respects.

First, in the typical power purchase agreement, the parties are private actors who enter into the agreement voluntarily. The State does not decide who will be the seller; nor does it force anyone to be the buyer. The parties to a typical power purchase agreement choose each other; they are not chosen by the State.

Second, the parties to the typical power purchase agreement set their own terms, including the price. They freely negotiate what price the seller (*e.g.*, the generator) will receive in exchange for title to the power. And the seller receives that price regardless of what the buyer (*e.g.*, the distribution company or

utility) does with the power it purchases. The utility could decide, for instance, to sell the purchased power into the PJM market. Whatever the PJM clearing price turns out to be, the utility must still pay the generator the price under the power purchase agreement. That is the price the utility agreed to pay; it is an amount freely negotiated by the parties—not dictated by the State.

In short, private power purchase agreements are voluntary agreements, while the CfDs in this case are not. That matters, because only *state* action is subject to preemption. *See supra* pp. 4-5. The typical power purchase agreement does not involve state action in either its negotiation or its formation. And absent state action, there is nothing for the FPA to preempt. Thus, if this Court were to rule (as it should) that the state-ordered CfDs in this case are preempted, that holding should have no bearing on the ability of private actors to enter voluntarily into power purchase agreements.[5]

3. This is not to say that private parties' power purchase agreements are beyond FERC's jurisdiction. The fact that the typical agreement does not involve state action in either its negotiation or its formation means that it cannot be subject to *preemption*. But that does not mean that it cannot be subject to *regulation*. Because these private agreements

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[5] None of this is to suggest that the State could have avoided preemption in this case if it had *ordered* parties to enter into power purchase agreements instead of CfDs. If the State had *ordered* parties to enter into power purchase agreements with terms like the CfDs, those agreements would also be preempted: They, too, would constitute state action aimed at wholesale rates.

are contracts for the sale of electricity at wholesale, FERC has authority under the FPA to review them and decide whether their prices are "just and reasonable." 16 U.S.C. § 824d(a). Pursuant to this authority, "FERC may abrogate" such a bilateral agreement "if it harms the public interest." *Morgan Stanley*, 554 U.S. at 548. In addition, FERC may "set aside a contract where there is unfair dealing at the contract formation stage—for instance, if it finds traditional grounds for abrogation of the contract such as fraud or duress." *Id.* at 547.

Thus, as a voluntary contract for the sale of electricity at wholesale, the typical power purchase agreement is not subject to preemption, but is subject to FERC's review and regulation. Among the agreements of this type that FERC has reviewed—and accepted as valid—is AEP Ohio's agreement to purchase power from the Ohio Valley Electric Corporation (OVEC). *See Ohio Valley Elec. Corp.*, Letter Order in FERC Docket Nos. ER04-1026-000, *et al.* (Dec. 13, 2004) (accepting Amended and Restated Inter-Company Power Agreement); *Ohio Valley Elec. Corp.*, Letter Order in FERC Docket Nos. ER11-3181-000, *et al.* (May 23, 2011) (accepting extension of OVEC agreement).

B. A State May Allow A Utility To Pass Certain Costs Of A Power Purchase Agreement On To Consumers Because Such Action By The State Is Aimed Only At The Retail Rates Consumers Pay.

Either before or after a private power purchase agreement is finally executed, a utility might ask a state public utilities commission for retail-rate treatment. That is, a utility might ask the state

commission for permission to pass the costs and revenues of the agreement on to retail ratepayers—*i.e.*, consumers. For example, if the utility bids its purchased power into the PJM capacity market and the PJM clearing price turns out to be *lower* than the agreement's price, the utility might seek to recover the amount of that difference by charging consumers a higher retail rate. Similarly, if the PJM clearing price turned out to be *higher* than the agreement's price, the utility might seek to give consumers a credit in the amount of that difference.

In deciding whether to permit retail-rate recovery for the costs of a private power purchase agreement, a state commission typically conducts what is known as prudence review: It reviews the prudence of the utility's actions, including its decision to enter into the agreement and the price at which it chose to bid its units of purchased power into the PJM market. If the state commission concludes that the utility's actions were prudent, it will then allow the agreement's costs to be incorporated into the retail rates that the utility charges consumers.

A state commission's order permitting or denying retail-rate recovery is a form of state action. But unlike the state action in this case, it is state action that is traditionally aimed only at retail rates. The commission's review would be limited to deciding what the retail rate should be in light of the utility's costs and other considerations concerning retail customers. Because that traditional type of review would not involve second-guessing the reasonableness of any wholesale rate, a commission's order approving or disapproving the pass-through of certain costs to retail customers would be permissible. *See Pike Cty. Light & Power Co.-Elec. Div.* v. *Pa.*

Pub. Util. Comm'n, 465 A.2d 735, 738 (Pa. Commw. Ct. 1983) (distinguishing FERC's jurisdiction "to determine whether it is just and reasonable *for* [*a power supplier*] *to charge* a particular rate" from a state commission's jurisdiction to determine "whether it is just and reasonable *for* [*a utility*] *to incur* such a rate as an expense"); *Pub. Serv. Co. of N.H.* v. *Patch*, 167 F.3d 29, 35 (1st Cir. 1998) (similar); *Ky.-W. Va. Gas Co.* v. *Pa. Pub. Util. Comm'n*, 837 F.2d 600, 609 (3d Cir. 1988) (similar); *Cent. Vt. Pub. Serv. Corp.*, 84 FERC ¶ 61,194, ¶ 61,975 (1998) (endorsing the *Pike County* doctrine); *cf. Nantahala Power*, 476 U.S. at 972 (assuming, without deciding, that States may consider whether a wholesale purchase is excessive "if lower cost power is available elsewhere").

Indeed, by aiming its review directly at retail rates, the state commission would avoid *dictating* any actions in the wholesale market. Whether the commission approved retail-rate recovery or not, the prices, terms, and conditions of the power purchase agreement would continue to be set by the parties who voluntarily opted to enter into that agreement on their own terms. The utilities would continue to have the ultimate say over the price at which they offer the purchased power into the PJM markets. And the amount of compensation that they receive in exchange for that power would continue to be determined by the relevant pricing mechanism in the market—for instance, the Reliability Pricing Model in the capacity market.

To be sure, the state commission's willingness to permit retail-rate recovery might *affect* whether the utility decides to enter into a power purchase agreement, or the price at which the utility decides to bid into the PJM market. But that does not mean that

such retail-rate treatment is preempted. As this Court has explained, preemption cannot rest on mere effects on the wholesale market, because all sorts of "'traditional' state regulation" have such effects. *Oneok*, 135 S. Ct. at 1600. In *Oneok*, for example, there was no dispute that state regulation of the practices at issue would have "affected wholesale * * * rates." *Id.* at 1599. And yet, the Court held that application of the state laws was not preempted, because the laws were "directed at" subjects on the retail, as opposed to the wholesale, side of the line. *Id.* at 1599-1600. So too here. Even if a state commission's approval of retail-rate recovery had some indirect effect on wholesale decisions, it would not be preempted, for that action would nevertheless be directed at retail rates.

To conclude otherwise would call into question well-established precedent and practice. State commissions have a long history of reviewing the prudence of utilities' wholesale purchases for the limited purpose of deciding whether to permit retail-rate recovery. *See Pike Cty.*, 465 A.2d at 738; *Patch*, 167 F.3d at 35; *Ky.-W. Va. Gas*, 837 F.2d at 609. When Congress enacted the FPA, it plainly did not intend to preempt the "continued exercise" of that traditional "state power," aimed directly at retail rates. *Oneok*, 135 S. Ct. at 1601 (internal quotation marks omitted). Moreover, the FPA undisputedly does not preempt retail-rate recovery for costs borne by utilities when generating power through their own plants—as in the case of vertically integrated utilities, which still exist throughout the Nation, including in States within PJM's own markets. There is no reason the result should be any different

when the utility incurs costs obtaining power through a power purchase agreement instead.

In sum, to the extent there is any state action involved in private power purchase agreements, it is traditionally "directed at" retail rates, which are "firmly on the States' side of [the] dividing line." *Id.* at 1600 (internal quotation marks omitted). Thus, this Court should conclude that the state-ordered CfDs in this case are preempted, but it should not issue an opinion that stands in the way of private actors voluntarily negotiating and entering into power purchase agreements and obtaining retail-rate recovery of the costs. No issue regarding such private power purchase agreements is presented by this case.

CONCLUSION

The judgment of the Court of Appeals for the Fourth Circuit should be affirmed.

Respectfully submitted,

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